BEFORE THE ARIZONA CORPORATION COMMISSION

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CHAIRMAN
RENZ D. JENNINGS
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IN THE MATTER OF THE COMPETITION IN THE PROVISION OF ELECTRIC SERVICES THROUGHOUT THE STATE OF ARIZONA.	DOCKET NO. RE-00000C-94-0165

REPLY BRIEF OF INTERVENORS AJO IMPROVEMENT COMPANY, MORENCI WATER & ELECTRIC COMPANY AND PHELPS DODGE CORPORATION

DATED: March 23, 1998.

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INTRODUCTION

This Reply Brief is organized into the following sections: (1) Absence of a So-Called Regulatory Compact as a Basis for Utilities' Claimed Entitlement to Stranded Costs; (2) Reply to Utilities' Initial Briefs; and (3) Reply to Other Parties' Initial Briefs. The same abbreviations and conventions have been used concerning citation form and references to parties. Collectively, AIC, MWE and PD are sometimes referred to herein as "Intervenors".

I. Absence of a So-Called Regulatory Compact as a Basis for Utilities' Claimed Entitlement to Stranded Costs.

A. The Assertion of a "Regulatory Compact" is a Prohibited Collateral Attack on a Final Commission Decision; The Phrase is Merely an Inaccurate Description of Part of the Policy of Regulation.

As stated in our Initial Brief, the Commission has rejected the claim that the Electric Competition Rules ("Rules") are precluded because of a so-called "regulatory compact." Decision No. 59943, pp. 36-37. Two Maricopa County Superior Court judges have agreed with the Commission. See Tucson Electric Power Company v. Arizona Corporation Commission, No. CV 97-03748, et. al. (consolidated). Minute Entry Order dated November 19, 1997, p. 5; Arizona Electric Power Cooperative, Inc. v. Arizona Corporation Commission, No. CV 97-03920 (consolidated). Minute Entry Order dated January 16, 1998, p.9. All parties who assert the existence of such a "compact" are contravening the Commission's final order and the court decisions in violation of A.R.S. § 40-252. Such assertions are also barred by the doctrines of res judicata and law of the case. They cannot be considered by the Commission as a matter of law.

It should be noted that the term "regulatory compact" is a partial description of some of the principles underlying utility regulation in general. It is an incorrect description, however, since as phrased by the utilities, the "compact" amounts to an "entitlement" to recover "full" uneconomic costs. Under public utility regulation, utilities have never been allowed to roam in a "cost plus" atmosphere.[1] There is no automatic "entitlement" to recover any (let alone "full") uneconomic investments. Specifically, as to utility investment that has become uneconomic because of the forces of competition, the state is under no obligation to allow the recovery of uneconomic investment in rates for a utility. Quite the opposite is true and the regulator need not allow a utility's investment in rate base that has been impaired because of competition. Market St. Ry. Co. v. Railroad Comm'n. of California, 324 U.S. 548, 567 (1945); Public Serv. Comm'n. of Montana v. Great Northern Utils. Co., 289 U.S. 130, 135 (1933). This is merely an offshoot of the principle that private enterprise does not have a constitutional right to be insulated from competition. Tennessee Elec. Power Co. v. Tennessee Valley Authority, 306 U.S. 118, 139 (1939).

The utilities' assertions fly in the face of these well settled constitutional principles and should be rejected.

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[1] Specifically, APS has been criticized in the past for having a "cost plus mentality." In the Matter of the Application of Arizona Public Service Company, Decision No. 46512 (October 30, 1975) at p. 4 ("It should be clearly understood that this Commission will not condone a 'cost plus mentality' in the management of any utility under our jurisdiction.")

II. Reply to Utilities' Initial Briefs.

A. Reply to Brief of Arizona Public Service Company.

1. Ratepayers Did Not Create the Abundance of Capacity in the Region and Are Not the Indemnitors of Utility Investment.

APS states that "stranded costs will, for the most part, result from the oversupply of capacity and energy in the Western Systems Coordinating Council ("WSCC")." APS Initial Brief at p. 8. Mr. Davis testified: "The largest cause of stranded cost is the current market imbalance caused by the relative oversupply of capacity and energy in the [WSCC]." APS Exhibit 8, p. 10, lines 12-14. It is important to note that the ratepayers did not create this oversupply condition. Decisions to build high cost generation facilities were made by the management of utilities. If those decisions did not correctly anticipate that technology advances would make these existing generation facilities uneconomic, the ratepayers should not be called upon to make up the loss. Ratepayers have never been insurers or indemnitors of utility investment. Los Angeles Gas and Elec. Corp. v. Railroad Comm'n. of California, 289 U.S. 287, 306 (1933); Market St. Ry. Co. v. Railroad Comm'n. of California, supra.

What is now required in a transition to competition is the Commission's exercise of its constitutional authority to establish a rate or recovery mechanism that fairly and reasonably balances all relevant factors, Simms v. Round Valley Light & Power Co., 80 Ariz. 145, 151, 294 P.2d 378, 384 (1956), including the interests of shareowners and the interests of the ratepayers. This balancing obviously gives the Commission the authority within its range of

legislative discretion to reject the utilities' claim for an "entitlement" to "full" collection of strandable costs and craft a result that is fair, reasonable and in the public interest. Certainly, a decision which would place the utilities "at risk" for non-recovery as an incentive to mitigate their strandable cost exposure is not a "disallowance" in any respect. Such a result would correctly reflect the Commission's constitutional balancing of all relevant factors.

2. The APS "Look Back" Proposal Amounts to an Unfair Guarantee.

There are many objections to APS' eight year "look back" proposal. First, the ratepayers would act as indemnitors and pay for 100% of the costs of enabling APS to become the "big dog" in the generation marketplace of the future. This would be a perverse application of the Commission's constitutional duty of balancing all relevant interests. It would amount to a completely one-sided, shareholder-tilted insurance policy for the utilities. During the transition period, APS or other Affected Utilities would receive the same revenues - with or without competition! Second, the proposal incorporates a myriad of "operating costs" into the calculation in a fashion that provides the utility with an incentive to increase -- not decrease -- its costs. Why would any right thinking utility cut a dollar of its operating costs if to do so would deprive it of a dollar of stranded costs? Third, Arizona customers would be locked into the California Power Exchange price which will be driven by factors affecting California not Arizona. Fourth, under the APS

proposal, ratepayers would finance recovery of a utility's uneconomic costs and overpay because the market price is depressed (the lower the market price, the higher the utility's stranded costs). Then at the end of the transition period, the utility could sell the facilities and reap all profits. Fifth, a provision for annual recovery of all uneconomic capital costs, would allow the utility an unfair advantage during the transition period to compete at marginal costs of operation (since its capital costs are being recovered through the stranded cost charge) while competitors must try to recover all of their costs. Sixth, the proposal involves the added headache of annual rate cases. Seventh, under the APS proposal, the stranded cost charge would vary on a yearly basis providing no certainty for competitors to plan for the future. The foregoing and other deficiencies in the APS plan (as identified in the briefs of other parties) demonstrate that it would be a "business as usual" method under which the ratepayers would be called upon to pick up the tab to finance bringing APS into the world of competition over an unduly long eight year period.

3. The Rules' Current Definition of Mitigation is Neither "Nonsensical" Nor "Perfectionist".

APS complains that the Rules' current definition sets a "nonsensical" and "perfectionist" standard. APS Initial Brief at p. 11. This complaint is misplaced and unsupported. APS' asserted interpretation of the Rule has been carried to illogical extremes. In fact, the Rules' "every feasible" requirement sends the only proper message to utilities. It recognizes that stranded cost

charges are extraordinary and must be reduced or eliminated as much as possible. The standard should be high because stranded costs act as an impediment to the emergence of competition. AECC, et. al., Exhibit 2, p. 7, lines 12-16 (Dr. Rosenberg). The objective of the Rule is to move to competition in an orderly fashion and to encourage competitive generation to occur sooner rather than later. The utilities must accomplish everything that they can in order to mitigate stranded costs.

This is not at all a "contract" issue analogous to "mitigation of damages." As evident from this and other parties' briefs (and two court decisions affirming the Commission's action), there are no contracts involved. The mitigation rule announced by the Commission is a policy standard that requires high efforts by utilities to reduce their strandable costs. The rule provides the proper signals and should not be amended as APS and other utilities propose. As a matter of public interest, the utilities must do everything they can to reduce or eliminate their strandable cost exposure.

4. The Market Price for Competitive Generation Must Reasonably Include Costs Above the Bus Bar Generation Cost.

APS quotes Dr. Hieronymus as chastising all of the uneducated masses who maintain that a market index price should not be the proxy for the price of competitive generation. We believe Dr. Hieronymus is wrong. AECC, et. al., including intervenors AIC, MWE and PD are not maintaining that all retail costs must be added to a particular generation price index. Rather, our position is a

recognition that one utility's bus bar production cost is simply never going to equate to a market price at which any retail customer could hope to purchase energy. The proper proxy must recognize that an energy marketer or new entrant will charge a mark up over that generation cost. There will also be ancillary charges involved. The market indices promoted by APS (the California PX) and TEP (the Dow Jones Palo Verde Index) do not factor these additional costs into the quoted price. Moreover, the "market price" for generation should reflect customers' preferences to line up a longer term (i.e., possibly a year or more) for the purchase commitment for competitive generation so as not to be whip-sawed by volatile changes in spot markets. A longer term preference would most surely reflect a price higher than spot or short term indices such as those advocated by the utilities. Adjustments need to be made to indices in order to provide a better proxy for a competitive price for generation in Arizona.

5. The "Sharing" Issue.

APS maintains that it would be arbitrary and capricious if the Commission did anything other than give the utilities what they want. This argument starts from the untenable premise that the utilities are "entitled" to a blank check. This has never been the law as demonstrated in our Initial Brief at pp. 2-8 and the Staff's Initial Brief at pp. 11-22. If this position were to be adopted, it would amount to a complete abdication of the Commission's constitutional responsibility to balance the interests of owners and consumers. A decision which would place the utilities (looked at on

a case-by-case basis) at risk for some of their claimed strandable costs would be fully supported by the Arizona and United States Constitutions and applicable case law. Importantly, APS has cited no legal authority to the contrary -- only the non-legal musings of Dr. Landon, a witness who did not recall whether Arizona was a fair value jurisdiction.

Some witnesses have used the term "sharing" in their presentations. However, it may be more accurate to say that the Commission in the exercise of its legislative ratemaking function may constitutionally decide that utilities should be at risk for some of the uneconomic costs occurring because of competition. It should also be emphasized that the Commission is fully empowered to conduct a "revaluation" of the property of any public service corporation at any time. A.R.S. § 40-251. ("For the purpose of ascertaining matters concerning the valuation or revaluation of the property of public service corporations, the Commission may conduct hearings at times or places it designates.") (Emphasis added.) If the "fair value" of the utilities' properties has been impaired because of competition, the Commission can revalue the properties in establishing a stranded cost charge or a general rate proceeding.

B. Reply to TEP's Initial Brief.

1. Assertions Concerning the "Regulatory Compact" are Erroneous.

Intervenors AIC, MWE and PD incorporate by reference pages 2-8 of their Initial Brief and join with the Staff in maintaining that TEP's assertions concerning the so-called "regulatory contract"

are prohibited collateral attacks on Commission Decision No. 59943. They are barred by res judicata and law of the case as well and cannot be relitigated. Judge Campbell's November 16, 1997 order speaks for itself. We reject the "spin" proposed in TEP's brief to be attached to Judge Campbell's order. The assertion of a "compact" or "contract" as a bar to the Rules was categorically rejected.

2. Use of the Net Revenues Lost Method for Calculating Stranded Costs is Flawed.

In our Initial Brief (pp. 14-17), we pointed out a host of problems with the net revenues lost approach. Other parties have cited the same and other notable problems. See, e.g., Initial Brief of EEC and Enron at pp. 14-25. There simply is no good reason to adopt a method that is filled with speculation and proceeds erroneously from the standpoint that the utility is entitled to be treated in a "business as usual" fashion. Hybrid methods such as proposed by AECC's, et. al. Mr. Higgins or by Staff's Dr. Rose are much preferred and provide the correct policy incentives to reduce or eliminate stranded costs.

C. Reply to Citizens' Initial Brief.

1. The "Regulatory Compact" Assertion.

In reply to Citizens' legal memorandum pp. 1-8, Intervenors AIC, MWE and PD incorporate by reference their positions and legal authorities previously cited here and in their Initial Brief. Citizens' assertion is a prohibited collateral attack on a final Commission order and should be rejected.

2. Citizens' "Takings" and "Confiscatory Rates" Arguments are Unripe and Premature.

Borrowing almost entirely from its legal brief pending in Superior Court in an action it now wants to voluntarily dismiss, Citizens asserts that a "taking" will occur or a "confiscatory rate" will result unless Citizens gets an opportunity for "full stranded cost recovery." Citizens' Memorandum, pp. 8-14. First, as stated above, there is no basis, constitutional or otherwise, to claim an "entitlement" to "full stranded cost recovery." At some point in the future, the Commission, in the exercise of its plenary ratemaking power, will consider and determine whether and to what extent Citizens is entitled to recovery of any so-called stranded costs. Until that happens, Citizens' protestations are premature and unripe.

3. Citizens' Desire to Shield its Wholesale Contract With APS from Review is Understandable.

In Citizens' stranded cost filing, the Commission will surely review the wholesale purchased power arrangement between Citizens and APS. Whether and to what extent that arrangement may be revisited is an issue that must await Citizens' utility-specific filing for recovery of its claimed stranded costs. That matter is not a "generic issue" for consideration in this proceeding. However, it is clear that state regulatory authorities may investigate the reasonableness of wholesale purchased power agreements even where they have been approved by the Federal Energy Regulatory Commission. Pike County Light and Power Co. v. Pennsylvania Pub. Util. Comm'n., 465 A.2d 735 (Pa. 1983). The Commission may disagree with Citizens' claim that the rule of Pike County is not applicable and the

Commission cannot investigate the prudence of extension or renewal of long term purchased power contracts. That debate must await the filing of Citizens' application for recovery of stranded costs.

4. Citizens' Claim for a Uniform Statewide Surcharge to Recover All Stranded Costs of All Utilities, if Not Abandoned, is Not Supported by the Record and is Bad Public Policy.

It is unclear from Citizens' brief whether it continues ill-advisedly to urge the Commission to adopt a uniform statewide surcharge to recover the pooled stranded costs of all utilities. That position appears to have been abandoned. Compare CUC Exhibit 1, p. 28 with Citizens' Initial Brief at pp. 25-26. If the claim for a single one-size-fits-all surcharge has not yet been abandoned, it should be. The proposal lacks any support whatsoever in the record, penalizes customers of the efficient utility, makes no sense and is bad public policy. See Intervenors' Initial Brief at pp. 9-14.

5. Citizens' Position on Burden of Proof Stands Utility Ratemaking on its Head.

Citizens advocates that the burden of proof should be on the parties seeking disallowance of a utilities' uneconomic costs. The Rules do not provide for any such burden and clearly envision that the burden of proof will fall squarely on the utilities to prove all aspects of the reasonableness of their stranded cost claims. Specific provisions of the Rules point to this being a high burden in view of the extraordinary nature of the claim. For example, Rule 1607(G) provides that utilities: "shall file estimates of unmitigated Stranded Cost. Such estimates shall be fully supported by analysis and by records..." (emphasis added). The eleven criteria specified

by Rule 1607(I) also envision that the utilities must be convincing in their presentations.

A.R.S. § 40-250 establishes that the burden in a utility rate filing is on the utility. The utilities' filing will constitute a request for a change in rates which may not be granted unless it is justified. See also A.R.S. § 40-203.

Citizens' proposal to shift that burden from the utilities to the Staff and intervenors should be rejected. To the extent that this matter may need clarification, Dr. Coyle's proposal on behalf of the City of Tucson should be adopted with an additional provision that recognizes that the burden of proof for recovery of strandable costs is high. See Intervenors' Initial Brief at pp. 11-14.

6. Citizens' Modification of its Auction and Divestiture Approach is Untimely.

Under the procedural orders governing the conduct of this proceeding, each party was to answer with specificity its positions concerning the eleven questions posed. See Procedural Order dated December 1, 1997 at p. 2. The Affected Utilities were to provide their responses in an initial filing in January and other parties' rebuttal filings followed. The original time frames for testimony filings were amended by subsequent orders. In its Post-Hearing Brief, Citizens has presented for the first time a new nine point position on auction and divestiture. No witness in the proceeding will be provided any opportunity to comment on such proposal because the hearings and the record are now closed. Although we agree that a market based method of computing strandable costs is preferred, in

fairness to all of the parties to the docket who thought that Citizens' positions were identified, the Commission should not entertain the consideration of Citizens' new position. It is untimely and in violation of the procedural orders.

7. Citizens' "Buy Out" of the Regulatory Compact Concept is Baseless.

Citizens maintains that a "useful analogy" from contract law supports the notion that one party to a contract that "wishes to be relieved of its obligations" can "with the consent of the other party, buy out the contract." Citizens' Initial Brief at pp. 7-8. Citizens' vision of this matter is blurry at best. First, there is no "contract" as demonstrated herein, in our Initial Brief, in Staff's Initial Brief and in the decisions of two judges of the Superior Court. Second, Citizens maintains that the alleged "contract" (here, the so-called "regulatory compact") is between the utilities and the Commission. Under the "buy out the contract" notion, therefore, the Commission (or the State of Arizona) would be the party who would be paying for a "buy out". It is undeniable that under this scenario, the Commission (or the State) would not "consent" to the "buy out" since it does not have a contract to begin with. It is even more undeniable that no consumers (whose "consent" would likewise be required under this notion) would ever agree that they had any obligation to bail out the Commission's asserted obligations, even if they existed (and they do not). So the whole concept goes nowhere.

Another fatal flaw in the "buy out" notion is that it is really a "bail out" concept that has been rejected by the United States Supreme Court. The State has no obligation to protect utilities from the consequences of competition. Market St. Ry. Co. v. Railroad Comm'n. of California, 324 U.S. 548, 567 (1945).

Citizens' contract buy out notion is not a "useful analogy;" it is simply not applicable.

8. Citizens' So-Called "New Function" Costs Are Not Includable as Strandable Costs.

Citizens maintains that with the advent of competition it will have to incur certain "new function" costs. Such costs are unknown future costs that do not yet even exist, unlike existing investments which may become uneconomic or strandable as a result of competition. They clearly are not within the general definitions of stranded cost either used in the present Rule or as discussed in the testimony of the witnesses. If they are ever incurred, they could be considered, if at all, only in the context of developing the tariffs for unbundled distribution service, unrelated to generation. These costs are not properly strandable in any respect.

In fact, Citizens itself maintains that these very same "new function" costs should be assigned for recovery as a part of its unbundled distribution activities. In its unbundled tariff filing made on December 31, 1997, Citizens seeks recovery of these same "new function" costs as a cost of local distribution. See page 44 of Citizens' Unbundled Tariff Filing dated December 31, 1997, attached

hereto at Tab 1.[2] At page 14 of Citizens' Initial Brief, lines 1-11, the same costs are defined and urged for recovery (using identical language) as a part of the definition of stranded costs. Obviously, Citizens cannot recover the same costs twice and Mr. Breen admitted as much during the hearings. TR 150. It is somewhat unusual, however, to be arguing for the recovery of the same costs simultaneously in two separate proceedings -- calling them local distribution company costs in one docket and asking that they be recovered as stranded costs in another.

Since these so-called new function costs do not even exist and they are unrelated to generation (as admitted by Citizens at p. 14 of the Initial Brief, lines 11-13), they cannot properly be considered to be a part of stranded costs.

D. Reply to AEPCO's Initial Brief.

The Commission should reject AEPCO's position concerning use of the net revenues lost method for calculating stranded costs for reasons set forth above and in Intervenors' Initial Brief. The Commission also should not recognize the "prudence exclusion" suggestion made by AEPCO. To do so would violate the Commission's constitutional obligations. Market St. Ry. Co. v. Railroad Comm'n. of California, supra, 324 U.S. at 567 (ratepayers do not "insure" values "that have been lost by the operation of economic forces" even if the investments were "once prudently made"). In addition, at any reasonable time, the Commission is entitled to conduct hearings

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[2] During the hearing on February 9, 1998, administrative notice was taken of Citizens' Unbundled Tariff Docket, TR 150.

concerning the "revaluation" of the property of any public service corporation under A.R.S. § 40-251. This statute plainly demonstrates that the Commission may at any time re-examine for sufficient reason the value of property once included in rate base.

III. Reply to Other Parties' Initial Briefs.

There were many positions taken by other parties in the proceeding on the eleven questions presented. Intervenors wish to provide specific comments on certain selected issues recognizing that time does not permit an individual reply to each party concerning each issue presented.

A. Stranded Costs Should Be Allocated in a Manner Consistent With the Specific Affected Utility's Current Rate Treatment of the Stranded Asset.

Some parties suggested that the recovery mechanism should allocate costs differently than the normal ratemaking cost allocation procedures used for the specific utilities. For example, certain parties proposed that stranded cost should be recovered through a KwH surcharge or a fixed fee. The Commission should resist any suggestion to depart from the established cost allocation principles that have been adopted for each specific utility in general rate proceedings. If any departure is contemplated, it would be necessary to reopen the rate design for all services and all rate classifications. Stranded cost should be recovered through a charge that is applied to the classes of applicable customers using Kw/KwH allocation principles that have been established and accepted as a part of the current approved tariffs of each of the Affected Utilities.

B. Special Contract Customers Should Be Excluded From Any Transition Charge Because They Do Not Participate in a Competitive Market.

Special contract customers are those customers who have a specific contract relationship with the utility to take bundled utility services at Commission approved rates. Because they are not participants in the competitive market, they should not be required to pay stranded cost charges beyond their current contract rates. In fact, contract customers are prevented under the rule from participating in the competitive market when their contracts are in effect, unless the parties otherwise agree R14-2-1604(F). As a group, such customers do not participate in the competitive market. Under the present rule, therefore, no stranded cost recovery from them is appropriate.

In the event that there is a change in the Rules, special contract customers can only become subject to stranded costs, if the Commission conducts the requisite proceeding under A.R.S. § 40-252 to alter or amend the decision that first approved the special contract. See also A.R.S. § 40-203. Under specific circumstances for a particular contract customer it may be possible to show that amounts paid under the contract were sufficient to constitute payment (or even overpayment) of the portion of stranded costs assigned to that customer by the utility. The special contract customer is entitled to the same due process protections under § 40-252 that the utilities claim apply to modifications of their certificates of convenience and necessity.

In fact, the Commission has normally treated special contract rates that have been approved as fixed and not affected by general rate cases. In Decision No. 59601, the Commission specifically excluded six special contract rate customers of APS from a general rate reduction. See Attachment No. 2 to Settlement Agreement approved in Decision No. 59601 (In the Matter of Arizona Public Service Company's Rate Reduction Agreement, April 24, 1996.)

Further, assuming arguendo a particular § 40-252 proceeding is conducted, and assuming the public interest required allocation of some stranded costs to a particular contract customer, it should be entitled to the same important protections that are applicable to all other classes of customers. First, the price paid to the utility for generation must be reduced by the amount of the transition charge so that the total price paid by the contract customer is not increased. Second, the Rules' existing treatment of self generation, demand side management and other demand reductions unrelated to competitive access must not be changed. It is possible that a portion of the special contract rate could be deemed to be a transition charge. The important point, however, is simply that special contract customers cannot be treated discriminatorily under the pretense of stranded cost recovery and could be included in the process only after the requisite hearing procedures set forth in the statutes have occurred. See A.R.S. § 40-252; 40-203.

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C. Self Generators and Interruptible Customers Should Not be Assessed Stranded Costs.

Self generation has always been a historic risk to the utility under the regulated regime. It therefore is totally inappropriate to assess to self generators any portion of a utility's claimed stranded costs. Rule 1607(J) currently exempts self generation from exposure to stranded cost surcharges. That Rule should not be changed. The rationale for excluding self generation and other demand reductions was fully debated in the process of adopting the original Rule. That rationale is sound.

Similarly, an interruptible customer does not receive the same service as compared to other customers. Such customers are at risk of interruptions of service by the utility. Interruptible service customers should not receive stranded cost charges. To do so would place an unfair burden on certain customers who have not contributed at all to a utility's stranded cost exposure.

CONCLUSION

For the reasons and authorities contained in the Initial Brief of AIC, MWE and PD, and the reasons stated herein, the positions of AECC, et. al. should be adopted in accordance with the summary of answers to the eleven questions presented attached at Tab 1 of Intervenors' Initial Brief. The Affected Utilities assertion of a "regulatory compact" should be rejected and the Commission should

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adopt a just and reasonable resolution to the question of strandable costs after balancing all relevant interests.

DATED: March 23, 1998.

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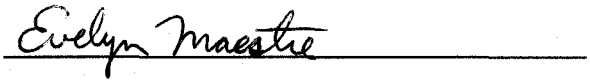

SECTION 3. NEW COSTS UNDER COMPETITIVE INDUSTRY STRUCTURE

Introducing competition in the supply of electricity fundamentally changes the structure of the industry, not only to the extent that it creates new competitive enterprise, but also that it changes the operations of those components that will remain regulated. For instance, continuous tracking, accounting, and reconciliation of energy supply and demand transactions between distribution customers and tens, possibly hundreds, of electricity suppliers requires the implementation and operation of new systems by local distribution companies ("LDC"s) that are not currently needed in their businesses. Educating customers about how the industry is changing and how these changes affect the way they will purchase electricity is another example of a significant new activity that will fall to the LDC to undertake. The costs for start-up and on-going operation of these functions are not currently reflected in the rates of any Arizona LDC, nor can any Arizona LDC accurately determine these costs at this time given that the structure and requirements of the restructured industry have not yet been fully defined.

A. The Nature Of The New Costs

At this time, it is not possible to determine with any certainty the exact nature, or the magnitude, of the new costs that LDCs will bear under the restructured industry. This is so because the full structure, requirements, and procedures under open access are still in flux. The ACC working group process conducted during 1997 succeeded in identifying and clarifying many issues and options associated with unbundled services and the operation of competitive industry, but at this time, the "rules of the game" are